



## NATIONAL CONGRESS FOR COMMUNITY ECONOMIC DEVELOPMENT

1030 15th Street, NW, Suite 325, Washington, DC 20005

Tel: 202/289-9020 Toll Free: 1-877-44-NCCED <http://www.ncced.org> Fax: 202/289-7051

July 2, 2001

Jeffrey Berg  
Acting Director  
Community Development Financial Institutions Fund  
U.S. Department of the Treasury  
601 13<sup>th</sup> Street, N.W.  
Suite 200 South  
Washington, DC 20005

Dear Mr. Berg:

The National Congress for Community Economic Development is pleased to submit comments on the advanced notice of proposed rulemaking issued by the Internal Revenue Service on the New Markets Tax Credit (NMTC). NCCED is a member of the New Markets Tax Credit Coalition and supports the comments made by that Coalition and signed by its convener, Robert Rapoza.

NCCED represents the nation's 3,600 community based development organizations (CDCs) that have developed more than \$71 million square feet of commercial and industrial space, created 247,000 jobs, and provided \$1.9 billion in loans outstanding (at the end of 1997) to 59,000 businesses. We expect CDCs to be successful users of the New Market Tax Credit program.

### **Section II. The New Markets Tax Credit Program: How the Credit Works**

*Timing of Allocation Agreements:* The guidance states that a Community Development Entity (CDE) may not issue any qualified equity investments to its investors until the CDE and the Fund have executed an Allocation Agreement. According to the draft guidance, an Allocation Agreement would specify the terms and conditions of the NMTC allocation to the CDE. While we understand why such a document needs to be finalized before a CDE can enter into transactions with investors, we want some assurance that the Fund will move in a timely manner in issuing Allocation Agreements once a CDE has been notified of their allocation. Regulations will require a CDE to use 'substantially all' of its cash in qualified low-income community investments soon after it has secured cash from investors and thus CDEs will need to develop a pipeline of qualified low-income community investments once they are notified of their allocation. Therefore, we recommend that the final regulations specify that the Fund will finalize Allocation Agreements within two months of a CDE being notified of an allocation award.

### **Section IV. Eligibility**

*Directly Serving Low-Income Communities:* The guidance indicates that in order to comply with the 'primary mission test' an entity must demonstrate a mission of "directly serving low-income

communities.” While the NMTC statute requires that the primary mission of a CDE be “serving or providing investments capital for low income communities or low-income person” there is no statutory reference to a direct service requirement. In fact, two of the qualified low-income community investment activities authorize a CDE to ‘indirectly’ serve low-income communities through the purchase of loans from CDEs or investing in or lending to CDEs. Therefore we recommend that the final guidance specify that a CDE can satisfy the ‘primary mission test’ by either directly or indirectly serving low-income communities.

*Community Accountability:* While the statute states that community accountability can be met by having residents serve on “any” governing or advisory board of the CDE, the guidance states that the “accountability requirement may be met if residents of low-income communities are represented on the governing or advisory board of the entity’s managing general partner or other controlling entity.” In addition, the guidance cites an example of accountability as having low-income people or residents of low-income communities on such a board.

Thus, the guidance suggests a much more restrictive definition of “accountability” than the Fund uses for its other programs. For example, under the CDFI core program, an entity can be certified as a CDFI if they have representatives of the “target market” on their governing board or use other approaches, such as an advisory board, focus group or community meetings. A CDFI applicant must provide a brief narrative of how they are meeting the accountability requirement in their application. We recommend that the Fund apply a similarly flexible accountability test for the Credit.

In addition, we recommend that the guidance definition of “representative of low-income community” be expanded to include people whose primary job or activity is serving or working in such areas, such as a business owner, clergy leader, or a CDC director, who may live elsewhere, but is representative of the community and aware its needs. The current guidance definition is limited to people who either are low-income or are residents of the low-income community.

Finally, we recommend that CDEs be treated as meeting the accountability test if a majority of their governing or advisory board (if they employ such an approach) meets the “representative test.”

#### *Bank Enterprise Award (BEA) Issue*

The draft guidance would disallow a depository institution from receiving a BEA award for the provision of financial assistance to a qualified low-income community business using cash derived from NMTC investments. We recommend that this prohibition be dropped from the final guidance and that financial institutions be permitted to use the BEA program in tandem with the NMTC. Both the NMTC and the BEA program are targeted to low-income communities that are in need of significant capital investment. Therefore, we see no reason to prohibit the programs from working together to encourage private investment in low-income community businesses. Both are relatively shallow subsidies that could greatly enhance the viability of a project.

While there is statutory language that limits the use of the NMTC with other federal tax subsidies, there is no prohibition against using the BEA program with the Credit.

## **Section V. Evaluation**

While we understand that evaluation of programs are important, the draft guidelines propose an evaluation process that could be unnecessarily time consuming. While we understand the Fund has a fiduciary responsibility to underwrite NMTC allocations and insure that CDE applicants are eligible and have the capacity to carry out a proposed Comprehensive Investment Plan, we encourage the Fund to recognize the market driven nature of the NMTC program. Once a CDE is certified and secures a NMTC allocation from the Fund, it will need to market the Credit to private investors who will do their own due diligence before investing in the CDE. A CDE will need to pass the scrutiny of both the Fund and their private investors before it can actually utilize the NMTC. In our experience with state tax credits (Neighborhood Assistance Programs in fourteen states), this “double scrutiny” greatly increases accountability and performance.

The draft guidelines require a CDE to supply a Comprehensive Investment Plan that provides historical information and a minimum five-year investment strategy. Upon receiving notice of an award of an allocation, a CDE must then negotiate and finalize its NMTC Allocation Agreement with the Fund. We are concerned that the application, evaluation, and final allocation processes will be onerous and could substantially delay the availability of the tax credits intended to spur new investment. Therefore, we suggest a streamlined application process for CDEs that have previously submitted their Comprehensive Investment Plan to the Fund for one of the other CDFI Fund program. In such cases, we also suggest that the Fund not conduct a site visit since we presume the Fund has constructed such visits in the past.

Our experience with state tax credits has found that the public sector and investors can have a very short attention span for deals, thus maximum flexibility to increase the involvement of the investors should be a priority. We also recommend that the Fund consider having two allocation windows per year. We anticipate significant demand for NMTC allocations and making allocations twice a year would ease the pressure on the Fund and allow greater flexibility to CDEs undertaking timely economic development deals. We expect significant involvement with state and private funds at the local level whose timeframes may not accommodate an annual cycle.

## **Section VII. Pending Issues**

### *1. Application Scoring and Priority Points*

The statute requires that the Secretary give preference to CDEs that have a track record in providing capital or technical assistance to disadvantaged businesses or communities **or** to CDEs that proposed to make qualified investments in one or more unrelated entities.

We believe the intent of the statute was to give equal treatment to these preferences and we recommend that the regulations clarify that a CDE can get preference for **either** track record or investing in unrelated businesses – not both.

In determining whether an applicant has a successful track record of providing capital or technical assistance to disadvantaged businesses including non-profit organizations, we recommend that the following factors be considered:

- The total amount of capital provided by the applicant through loans, investments or services to low income communities or disadvantaged businesses including non-profit organizations;
- The number of disadvantaged businesses that have received loans, investments or technical assistance from the applicant;
- The overall success rate of the applicant in providing capital to disadvantaged businesses or low income communities, measured in terms of loan loss rates, return on equity, and other financial measurements; and
- The ratio of activities that provide capital or technical assistance to disadvantaged businesses for the overall activities of the applicant. For instance, an organization that has provided \$10 million in capital, (all of it to disadvantaged businesses), should receive higher priority than an organization that has provided \$50 in capital to disadvantaged businesses, but for which that figure pales in comparison to overall capital provided of \$4 billion.

In addition, we recommend that a priority be given to CDEs that commit to use the NMTC in their application to attract the predominant share of their investments from unrelated sources. This priority should also be granted to drop-down funds as long as the CDE can show that its parent fund received its funding from unrelated sources. Such an incentive will ensure that the credit is used to develop new sources of investment capital for economic development. The Coalition believes that the NMTC was intended as an incentive to encourage new investment in low-income communities not as an additional subsidy for current investment efforts. Therefore, we encourage the Fund to provide an allocation to entities that make this commitment before they make allocations to entities that will be drawing investments from related sources.

### *2. Limits on Annual Allocations*

The Coalition urges the Fund to ensure that there is both geographic diversity in how NMTC allocations are distributed as well as diversity in the types of organizations and projects that will benefit from the Credit. We suggest that allocations be distributed amongst small local and mid-sized regional CDEs as well as larger regional and national entities. In addition, we encourage the distribution of Credit allocations amongst debt funds, venture funds, mixed use funds and single purpose funds.

We believe there should be limits to the amount of a NMTC allocation that may be awarded to any single applicant in a calendar year in order to ensure that the expected benefits of the NMTC program are extended throughout the country to a variety of low-income communities. We recommend that no single applicant be awarded an NMTC allocation in excess of 10 percent of the amount of the allocation available in that year.

### *3. Documenting Track Record and Impact*

In our response to question number 2, we suggested several criteria for the Fund to consider in evaluating a CDEs record of providing capital or technical assistance to disadvantaged businesses.

We discourage the Fund from developing standard performance criteria for all CDEs since individual CDE's will pursue different development goals depending on whether they are operating a venture fund, a loan fund or using the NMTC to develop a single facility or project.

There are many different types of measures that the Fund could use in evaluating the effectiveness of the NMTC and CDEs using the Credit. While some of these measures are easy to quantify and relatively universal, such as the number of loans or investments closed and the dollar amounts of those transactions, these measures do not truly calculate program outcomes or impacts.

Ultimately, the purpose of the NMTC program is to increase the supply of private capital to underserved parts of the country. Documenting the existing capital gaps and the ways that CDEs use the Credit to narrow these deficits and provide capital to 'new markets' would probably be the best way to begin evaluating the NMTC program. We believe that the Federal Home Loan Bank could be helpful in this area.

The state tax credit administrators have learned numerous lessons in operating community revitalization tax credit programs. One lesson has been that a relatively high proportion of the credits are never claimed (15-25 percent). This does not mean that credit was not used, but rather that the form from the investor was never submitted to the state treasury. The CDFI Fund and the IRS should be cognizant of this historical trend in determining how the credit is used. In addition, they recognize that credits reflect a paradigm shift and thus take time to be fully utilized. Flexibility and communication are critical to the success of the program.

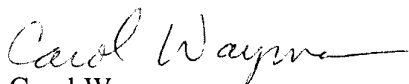
NCCED will be active with the New Markets Tax Credit Coalition in discussing the issue of program evaluation in more detail with the Fund. The NMTC is a market driven program aimed at increasing private investments in CDEs working in low-wealth communities. Therefore the evaluation criteria used in measuring impact and success will need to be different from those used by the Fund to measure the impact of its other economic development programs.

#### *4. Coordination with New Markets Venture Capital*

There should be some assurance that a certain number of New Markets Venture Companies (NMVCs) will receive the Credit, or the requirements for being a CDE should be considered met by NMVC Companies, as is the case in the new law for CDFIs and SSBICs.

We appreciate your consideration of these comments and look forward to working with the Fund as you move ahead in implementing the New Markets Tax Credit.

Sincerely,



Carol Wayman

Director of Policy Development and Research